Smaller is Better: Barriers to Building Affordable Multifamily Housing at a Neighborhood Scale

by

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Dedication

For Rodrigo, my handsome muse of really long papers.

Abstract

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Low- and moderate-income Americans rely on affordable housing. It is clear that affordable rental housing is needed, but much of what is getting built, especially in the high-growth West and South, gives rise to negative externalities based on the large number of units in the projects. This report looks at objections to large apartment complexes and makes the case for smaller-scale multifamily developments, studies how housing policy in the US has disadvantaged multifamily development, and investigates barriers to small-scale developments relating to mortgage markets, the Low Income Housing Tax Credit, and the models of nonprofit affordable housing providers.

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Chapter 1: Overview of the Issue

"You seem so out of context in this gaudy apartment complex"

The Postal Service - The District Sleeps Alone Tonight

SPECIFICATION OF THE CENTRAL FOCUS

The need for affordable rental housing in the United States is acute. According to the Millennial Housing Commission in 2002, in order to afford the median fair-market price of a two-bedroom rental unit in this country, a person would have to earn $12.47 per hour, or more than 240% of the current hourly minimum wage of $5.15. The Joint Center for Housing Studies found in 2003 that there is no county in America where a household with one wage earner at minimum wage can afford a modest one-bedroom apartment. Families who cannot afford to pay average rents make do by living in unsafe neighborhoods, doubling up with other families, moving frequently to get a better deal, or buying homes (such as mobile homes) that do not appreciate in value. These families are also forces to make difficult budget choices between food, medical care, clothing and transportation.

Low- and moderate-income Americans rely on affordable housing, in large part built either by owners supported by conventional mortgage markets or through the Low Income Housing Credit program, and often owned by nonprofit affordable housing providers. It is clear that affordable rental housing is needed, but much of what is getting built through these channels, especially in the high-growth West and South, gives rise to negative externalities based on the large number of units in the projects. Some are of a size and institutionalized design that isolates its residents, hearkening back to a now largely criticized style of government housing project. Many developments become subject to NIMBY-like criticism from area residents because they are out of scale with surrounding neighborhoods. Many developments are built on large plots of land away from the center city in order to offer a large number of apartments with affordable rents but their location ensures that residents will end up paying high transportation costs. Many multifamily developments interrupt the traditional fabric of cities that has for centuries given form to human interactions. This report will look more closely at the size of affordable multifamily housing developments by answering the following questions:

- What are the objections to large apartment complexes and the arguments in favor smaller-scale multifamily developments?
- What barriers exist to the creation of smaller-scale affordable multifamily housing?
- How can current policy and thinking be changed to better accommodate this desired smaller-scale model?

METHODOLOGY

In order to determine the specific objections to large apartment complexes and the arguments in favor of smaller-scale multifamily developments I relied on a wide range of sources. For information about urban design and the form of cities I drew heavily on books from some of the most influential modern urban thinkers, from Christopher Alexander and Jane Jacobs to Eran Ben-Joseph. To investigate the effects of large and small multifamily developments on social capital I studied scholarly articles from the Fannie Mae Foundation's Housing Policy Debate and looked at recent research from the Kirwan Institute's Opportunity Mapping program. Information about NIMBY reactions to affordable rental housing came from scholarly articles and my own experience with developments, and arguments regarding the high cost of transportation draw on publications from the Center for Neighborhood Technology and the Center for Transit Oriented Development.

In order to discover what barriers exist to the creation of smaller-scale affordable multifamily housing I first looked back in chapter three at how the history of the federal housing policy in the United States has support single family owner-occupied housing to the detriment of rental and multifamily housing by relying on a few important books by Gail Radford and Kenneth Jackson, supplemented by information from HUD and a series of articles in Housing Policy Debate published in 2000. To look more closely at barriers to small-scale housing I reviewed scholarly articles from publications such as HUD's Cityscape: A Journal of Policy

Development and Research and the Fannie Mae Foundation's Housing Policy Debate and reviewed reports, many of them commissioned or published by the US Department of Housing and Urban Development. Other information about barriers was provided by reports on the work of community development corporations, and an interview with an important local actor in Austin's affordable housing field.

Answers to the third question posed above – how current policy and thinking can be changed to better accommodate a smaller-scale model of affordable housing – came from all of these sources, and also draws on my personal experience working in affordable housing in Texas as an intern at two different nonprofit affordable housing organizations: Merced Housing Texas in San Antonio from June to August 2005, and Foundation Communities in Austin from June 2006 to the present. Though the geographic focus of this report is not specific to Texas and not all of my experiences as an intern are completely generalizable, I will throughout this report refer to experiences I encountered when I feel they illustrate broader issues.

In my research I have tried to maintain focus on the size (in number of units) of multifamily developments in order to investigate deeply one particular component of what constitutes good affordable housing – the case for which I will set out in the chapter that follows. Inevitably, however, the discussion about the size of developments bleeds into issues of housing location, design, and sometimes the age of structures and issues relating to rehabilitation versus new construction. These issues are hard to disentangle, and though the focus here is on the size or scale of projects, references to location and other factors cannot and should not be avoided.

In order to argue for smaller apartments, we must first define how large a "small" multifamily development is. The definition accepted by the United States Department of Housing and Urban Development (and used by other researchers) is that a small multifamily property consists of between 5 and 49 units (properties with under 5 units are considered single-family in nature).

CHAPTER OUTLINE

This report is divided into seven chapters, including this introduction. The second chapter will argue the importance of building affordable housing at the small scale that can fit into the fabric of a neighborhood focusing on four aspects: the form of cities, concentration and social capital, the relationship between transportation and housing costs, and neighborhood opposition to affordable housing. The third chapter discusses the history of housing policy in the United States, with a focus on federal policies that supported single-family housing to the detriment of multifamily development. The following series of three chapters examines and explains the factors promoting large-scale affordable housing developments. Chapters four and five focus on federal-level policies – the mortgage lending system and GSEs and the Low-Income Housing Tax Credit (LIHTC) program respectively – looking at their effect on multifamily development patters. Chapter six examines the emergence of community development corporations (CDCs) in the housing arena and looks at the ways in which CDCs are adapting to changing contexts. Chapter seven concludes the report with thoughts and recommendations for encouraging smaller-scale developments.

Chapter 2: Objections to Large Apartment Complexes and the Case for Smaller-scale Multifamily Developments

Though quality affordable rental housing is clearly needed in the United States, much of the housing produced, especially in the high-growth West and South, gives rise to negative externalities based on the large number of units in the projects. What are the objections to large apartment complexes and the arguments in favor smaller-scale multifamily developments? This chapter demonstrates the importance of building small-scale affordable housing focusing on four aspects: the form of cities, concentration and social capital, neighborhood opposition to affordable housing, and the relationship between transportation and housing costs.

URBAN DESIGN – THE FORM OF CITIES

In David Sucher's book *City Comforts*, he paraphrases noted author and urban thinker Christopher Alexander. Alexander believed that cities did not come into existence solely for the historically accepted reasons of politics, trade, and security. For Alexander, cities exist to facilitate human contact and closeness, and the success or failure of a city or an urban place can be judged by how well or poorly human contact is encouraged – "physical form is only a means to an end. The means are buildings and roads and parks. The end is improved relations between people" (Sucher, 17). Panerai, et al. agree on the important social role that cities play, insisting "the understanding of architectural and urban forms is as legitimate and effective a means of understanding a society as any other" (x).

So how can we build our cities to facilitate human interaction? Panerai and the other authors of *Urban Forms: The Death and Life of the Urban Block* suggest starting by recognizing the role buildings and their placement have on the public realm. Beginning in the middle of the last century, the public realm became "sort of a no-man's-land" between the disciplines of architecture, that had become "too concerned with individual special buildings," and planning, which "particularly in academic circles had become preoccupied with process and management, economics and social welfare, and any concern with physical form was perceived as being academically frivolous" (vi). The system of gridded blocks that had long held urban places together was ignored or distorted into Le Corbusier-style blocks consisting of single buildings. The block and the street lost their significance as transition spaces that simultaneously connect and separate what is small and personal from what larger and public (129). Without this structure, buildings are placed on sites without regard for concepts of 'front' or 'back', creating ambiguity that affects the use and ownership of the spaces between buildings (132, 175), resulting in "a process of the reduction of spatial experience exclusively to the dwelling itself, which was finally conceived as a distinct unit" and prompting Panerai, et al to cry "Where is the street, the city, the urban space?" (133).

Modern large-scale apartment complexes are an excellent example of the sort of development divorced from city blocks that creates ambiguous and unused spaces. Rectangular pods of eight to twelve apartments are placed diagonally by the dozen on large plots of land. According to Ben-Joseph, this strange urban form owes much to the Federal Housing Administration (FHA – discussed in more detail in the following chapter), the most significant force in the shaping of the form of residential development in the United States. The incentive-based programs run by the FHA beginning in the 1930s "always appeared to be non-coercive to the private sector". The FHA's standards were viewed as "private contracts which were freely entered into by willing parties – rather than as similar to zoning laws, which were sometimes seen as infringing on constitutional liberties" (Ben-Joseph, 70-71). Though the FHA claimed that it was not in the business of setting patterns of land development across the country, it did establish detailed regulations about such issues as setbacks widths, rejecting the grid pattern and taking away from the integrity of the urban block. In many instances these regulations "pushed developers to build in green-field locations, away from major urban areas, where restrictions and abutters' objections would be less severe" (112).

In order to restore the urban fabric into something that promotes human interaction, Panerai et al suggest a return to the basic form of the urban block. Their book describes blocks as tissue:

> The concept of tissue, in fact, with the double textile and biological connotations, evokes ideas of interweaving and of connections between parts, together with a capacity for adaptation…. It can provide a critical response to those problems that we have inherited from recent developments (158).

A city subdivided by blocks consisting of smaller plots is an adaptable city, allowing adaptation to the demographic, economic, and cultural changes that mark urban places: "Buildings can change on plots without affecting the overall plot arrangement, plots can be subdivided or amalgamated without affecting the form of the block and blocks can be modified without affecting the road network" (201). Jane Jacobs, another seminal urban thinker, agrees. In her landmark 1961 book *The Death and Life of Great American Cities*, Jacobs advocated the piecemeal redevelopment of buildings on existing blocks in existing neighborhoods as the best way to weave low-income housing into the tissue of the community.

Zooming out a little from the block, we return to Alexander's ideas about the form of cities. His book *A Pattern Language* argued for a mix of households and types of housing within any given neighborhood, based on the idea that a person should be able to go through their entire life cycle in one neighborhood without ever being inconvenienced or out of place. Though large apartment complexes can have a mix of unit types, they are more homogeneous than Alexander would endorse (143, 189), and do not fit with his vision of the importance of identifiable neighborhoods, which he and his co-authors quantify as consisting of between 500 and 1500 residents (81-82). A large modern apartment complex would dominate such a neighborhood if it could be considered part of one at all. Alexander would most likely classify large apartment buildings as the sort of monolithic developments he believed defy human social structures and fail to achieve the goal of cities: improved relations between people (469).

CONCENTRATION, ISOLATION, SOCIAL CAPITAL, AND OPPORTUNITY

Housing policy in the past in the United States created monolithic structures that defied the positive human interaction that Alexander believes cities were built to facilitate. The government housing projects built in the middle of the last century ghettoized poverty. They concentrated the poorest Americans in enormous mid- and high-rise apartment developments that did not support the formation of social capital among residents, and removed them from the urban fabric and access to opportunity.

Robert Putnam, the oft-cited civil society expert, defines social capital as "features of social organization, such as networks, norms, and trust, that facilitate coordination and cooperation for mutual benefit" (1993). These networks can be made within socio-economic strata, between residents of a single housing development. Some research shows that the size of the development is important. According to Putnam, "the evidence confirms that smaller is better from a social-capital point of view – i.e. getting involved is easier 'where the scale of everyday life is smaller and more intimate'" (2001, 179). Briggs and Mueller also found that

> Social relationships among neighbors [at a Whittier Alliance housing co-op in Minneapolis], enhanced by active tenant groups and the small scale of CDC buildings, enrich resident's psychological sense of connection to others and promote involvement in collective activities".

In this case the small size of the development was one factor contributing to the development of social capital among residents (other factors included the level of neighborhood crime and participation required by the co-op structure of the housing) (16-17).

Social capital can also be built across socio-economic strata. In his article "Rethinking the Social Role of Public Housing", Spence argues that "concentration of the most deprived families" should be avoided because of its negative effect on the creation of social capital (359). Though his focus is on public housing and the sort of affordable housing discussed in this report do not necessarily house the "most deprived" families, the Spence article highlights the importance the creation of links, both social and physical, between people at different income levels or different stages of life. In his words, such links connect the community living in affordable housing to "the social fabric of the surrounding neighborhood to relieve the 'institutional abandonment' that accelerates the decline of distressed developments" (362). Spence also argues that positive "neighborhood effects" are created by integrating housing for lower-income groups into the greater community and without those effects, "accelerating depletion of access to social capital" will result (366).

Another way to think about building social capital across socio-economic strata is being pioneered by john a. powell at the Ohio State University's Kirwan Institute for the Study of Race and Ethnicity. Termed "Opportunity Mapping," powell's method researches the geographical distribution of resources in a community (transportation, schools, health care, jobs, etc) and creates maps that "provide a visual representation to help a region understand how socio-economic opportunity is distributed throughout the community". These maps are intended for use by policymakers, giving them the data and vocabulary they need to shape policy to increase socio-economic equity. According to powell, the single most important aspect of Opportunity Mapping is the location of housing because "housing policy is social policy".

The size of housing developments does have bearing if a city attempts to move toward powell's vision of affordable housing connected to opportunities such as job centers, good schools, and safe neighborhoods. Smaller-scale affordable rental projects are easier to locate in high-opportunity neighborhoods than larger projects because they are subject to less Not-In-My-Backyard scrutiny by prospective neighbors.

COMBATING NIMBYISM

Residents of neighborhoods across the country have protested so often and so vehemently to proposed developments in their area that they have earned no less than three descriptive acronyms: CAVE for Citizens Against Virtually Everything, BANANA for Build Absolutely Nothing Anywhere Near Anything, and the best known NIMBY for Not In My BackYard. As the acronyms suggest, neighborhood residents resent development of any kind, but affordable housing, especially in the form of a large 'garden' style apartment complex, is so objectionable that developers often build developments alongside highways or large arterial roads away from residential areas in order to avoid complaining neighbors (Clark and Markson).

Neighborhoods object to affordable housing developments for many reasons, not the least of which is concern for the value of their property, and not wholly without reason. One study suggests that there can be a negative effect on nearby property values when the amount of public housing in the area reaches a "tipping point" (Warren). Other literature discusses the possibility of the "over saturation" of particular area of town with affordable housing developments, which leaves some neighborhoods feeling unfairly burdened. Neighborhood residents also worry about the affect of affordable housing developments on school quality (Galster). Because these projects are perceived as attracting a disproportionate number of families, and in many parts of the country pay reduced taxes to the school district, communities have opposed them claiming that schools will suffer with an influx of low-income children. Though recent research by the Danter Company showed that families living in affordable housing developed using tax credits actually have fewer school-age children than other nearby families, perceptions are difficult to change and the issue is still of significant concern.

Sucher recommends that the best way to convince NIMBY neighbors to accept any type of new development is to design something that they will like the look and feel of; Briggs suggests that there is less opposition to apartments that are well designed; Cummings and Landis explain that developments that blend into the community are better received by neighbors. Research has shown that scattered site housing does not have the same negative effects of larger single developments (Briggs). Building affordable housing at a neighborhood scale allows for increased access to opportunity for its residents with the least possible objection from its neighbors. Under these circumstances, affordable housing can actually be a boon to neighbors: “A policy of dispersed location of small-scale public housing projects in inherently viable neighborhoods, then, compensates local home owners for some degree of site-related disamenity with neighborhood amenity" such as an increase in service levels such as park events, public transportation, viable schools, consumers for local stores due to increased neighborhood population (Rabiega, 179).

TRANSPORTATION AND HOUSING COSTS

Along with reduced neighborhood NIMBYism, another benefit of small-scale affordable housing development is that it can fit more easily as an infill project into transit-rich neighborhoods near shopping, schools, and work. Though land values in such areas are often considered too high to feasibly produce affordable housing, advocacy groups and researchers now suggest that the traditional definition of what constitutes affordable housing is too limited, and that "it is the interaction between housing and location that provides a more meaningful measure of affordability" (CTOD, 2). Recent research has shown that contrary to previous beliefs, a household's transportation demand is not driven primarily by household income and size, but is instead highly correlated with neighborhood characteristics (CTOD). Transportation is the second largest household expense after housing, and though the average US household spends nearly 20 percent of its income on transportation, its costs "are often dramatically underestimated or ignored" (CTOD). The Center for Housing Policy (CHP) found that the high cost of transportation is a particular burden for working families, those families earning between $20,000 and $50,000 annually.

The CHP reports “for every dollar a working family saves on housing, it spends 77 cents more on transportation” and that housing and transportation costs combine to consume 57 percent of the household income of working families, with nearly equal proportions going to each (28 percent to housing and 29 percent to transportation).

When the high cost of transportation is combined with housing costs, the geographical picture of housing affordability changes dramatically. In a case study of four neighborhoods in Minneapolis-St. Paul, only central city neighborhoods were considered affordable for those households earning less than 50 percent AMI. The determining factors of affordability were better transit service which lowered transportation costs, access to more jobs, and the availability of some lower priced housing (CTOD). The study showed that neighborhoods closer to the city center were more affordable across the board than outlying areas, even though housing costs on average in these places was greater or equal to housing costs further out.

Though we are beginning to understand the impact of transportation costs on the affordability of housing locations, transportation costs are not considered by conventional lenders or by affordable housing programs such as LIHTC and vouchers, nor will they be in the absence of an effective tool to measure ‘true affordability’. The Center for Transit Oriented Development and the Center for Neighborhood Technology have come up with a tool that “prices the trade-offs that households make between housing and transportation costs” (1). The tool uses information from various sources to come up with a formula that divides housing costs added to transportation costs by income, on census block group level. Though still in its early phases, the Affordability Index idea can help policy makers and consumers to more fully understand the impact of housing location and its associated costs.

If policy makers begin to understand the affordability implications of housing locations, it could have a profound impact on the form of affordable housing. CTOD and CHP call for affordable housing providers to give greater weight to the transportation costs of neighborhoods and to invest accordingly by developing housing on infill sites in inner city and older suburban neighborhoods that are close to job centers. They, along with Nelson call for jurisdictions to develop housing policy in conjunction with transportation policy and to assist affordable housing producers by awarding incentives to development locating near transit lines and employment centers. Building on existing urban lots and working within existing neighborhoods has the potential to push down on the size of affordable housing developments.

Chapter 3: How Federal Housing Policy has Disadvantaged Rental Housing Development

In order to understand the forces acting in today's affordable multifamily market, and to fully appreciate the origin of the issues presented in the previous chapter, it is essential to study the history of housing policy in the United States. This chapter reviews the government's role in housing policy from its first interventions in the 1930s through the present time, and looks at the ways in which the government's role has contributed to American perceptions of housing. This chapter emphasizes the active role of the government as a supporter of single-family housing to the detriment of multifamily housing – an approach with specific impacts on today's discussions about affordable and multifamily housing policies.

DECLINE AND DEPRESSION

Prior to the Great Depression, the only government interventions in housing were measures imposed in large industrial cities to combat slum conditions by regulating ventilation, sanitation, and density. Federally funded housing in the United States had only ever been built for members of the military or to support military endeavors: during World War I the government constructed housing for shipyard workers whose jobs were considered critical to military success – "an exercise of the war power, not the disputed general welfare power" that would later provide the rational for government housing policies (Jackson, 192). Though "shelter was not regarded as an appropriate responsibility of government" (Jackson, 191) and that 'hands-off' federal role in housing did not change until the 1930s, housing shortages and quality problems were recognized long before the onset of the Depression. Throughout the 1920s, the costs of construction were rising because of a lack of lumber due to depleted timber stands in North America. Rising wages also pushed up the costs of housing construction more than in any other industry because labor costs comprises such a substantial portion of the cost of a house. Thanks to consumer demand for higher standards and more residential amenities, as well as the efforts of urban reformers like Chicago's Jane Addams, local building codes requiring a minimum standard of living were becoming stricter, which also contributed to rising housing costs. Between 1885 and 1925, the overall cost of living had almost doubled, but the price of an entry-level new home had more than quintupled. The basic housing problem was "a squeeze between modest, stagnant incomes and the rising costs of urban shelter" (Radford, 22). During the 1920s, many people connected to the housing field were beginning to speculate that "profit-driven activity would never solve the housing problems of a large proportion of the population" (Radford, 5). During that same period finance systems were changing in the United States. The Federal Reserve had been created, leading banks to invest more heavily than ever before in mortgage lending. More Americans were purchasing homes with long-term loans, rather than outright with cash (or with cash and short-term loans) as they had in the past. According to Radford, "While new sources of credit allowed some families to support higher housing costs, rising foreclosure rates well before the crash suggest that housing costs were simply too high in relation to incomes for many families" (56).

Though discussion about housing had been going on for a decade, the onset of the Great Depression made it a pressing public issue. Housing problems were no longer confined to low-income groups. Many middle class families were also struggling, which caused a domino effect throughout residential finance institutions. Banks were left holding the notes for many foreclosed homes and faced bankruptcy themselves (Radford, 86). The depression opened a policy window and allowed proposals for large-scale federal intervention in housing to appear on the agenda. For the first time, members of the middle class actively supported government intervention in housing, and "normally vigilant private real estate interests" that might have objected were "moribund at the national level" (Radford, 177).

In through this policy window stepped policy entrepreneurs from both ends of the ideological spectrum. On one side was a group of socially minded housing reformers that promoted following the European example of publicly financed and supported housing removed from the speculative market. Advocates of this 'modern housing' thought that with the help of cheap financing from the government, such housing could be built without subsidies (Radford, 78). Modern housing advocates were part of a wider movement that included organized labor groups and linked housing to other social reforms (Lang and Sohmer). Rather than serving only the bottom third of the population (unskilled workers), these advocates wanted the government to provide housing to two-thirds of the population, which would include the working and middle classes (von Hoffman, 301). Though these sorts of proposals "did not seem outlandish during the Great Depression when Americans were hard-pressed to obtain or keep their homes and the housing industry was in a serious slump" (von Hoffman, 301), political mobilization around them remained difficult. This was due in part to the American love affair with private property rights, defended most often and most vigorously by real estate interests. Under ordinary circumstances, these interests may have opposed any and all federal interventions into the housing arena. When the federal government did decide to intervene in housing during the Depression, however, real estate interests were concerned with getting out of their own precarious financial positions, and groups such as the National Association of Home Builders organized behind their own proposals for federal housing policy, opposing government-constructed housing in support of policies that would help private industry by strengthening financial markets (Jackson, 194).

Housing Acts: 1930s-1940s

The first permanent federal housing legislation, the Federal Home Loan Bank Act passed in 1932 by President Hoover, attacked the housing problem from the financial angle and by doing so garnered support from the real estate and mortgage lending lobbies. The act expanded the supply of housing capital by creating a system of federally supervised banks to support mortgage lenders. According to Radford, because of the crisis situation created by the Great Depression "a policy proposal that had seemed too extreme to make it out of committee a decade before was enthusiastically endorsed by the conference" (87).

When Franklin Roosevelt was elected president, he formed the Home Owners Loan Corporation (HOLC) to provide assistance to homeowners facing foreclosure – a brilliant political move that consolidated middle class support for his New Deal programs (Radford, 179). The HOLC "introduced perfected, and proved in practice the feasibility of the long-term, self-amortizing mortgage with uniform payments spread over the whole life of the debt " (Jackson, 196). The practices of the HOLC also systematized mortgage appraisal methods across the United States by using long lists of criteria and in-depth questionnaires in order to define the value of a house within a given neighborhood. The HOLC's appraisal methods gave more weight to a house's location rather than to the structure itself, and undervalued dense, mixed, or older areas in favor of new, homogeneous suburban neighborhoods (Jackson). The ideas and appraisal practices of the HOLC had an enormous influence on other financial institutions and their loan criteria, and were adopted by the Federal Housing Administration when it was created.

The HOLC did little to help the recovery of the real estate industry, so Roosevelt passed the National Housing Act of 1934, another finance-based solution to the housing crisis. This act established what some would argue is the most influential federal agency ever created - the Federal Housing Administration (FHA). According to Jackson, "no agency of the United States government has had a more pervasive and powerful impact on the American people over the last half century than the Federal Housing Administration" (203). The FHA to this day provides federally backed insurance for home mortgages and loans for owner-occupied housing rehabilitation. Creation of the FHA was intended to revive the housing industry and to provide much needed jobs in construction. Private financial institutions would issue the mortgages, and private builders would construct the new homes purchased with these mortgages (von Hoffman, 301). The FHA also brought mortgage capital to areas of the country that had not previously had access to it because the pockets of the local financial institutions were not deep enough to engage in mortgage lending (Martinez, 470). Throughout most of its existence, FHA practices discouraged the construction of multifamily housing by offering loan terms most favorable to single-family homes, making it cheaper to own then to rent, and often cheaper to buy a new tract home in the suburbs than to improve an older one (Jackson). Many middle and lower middle class families moved to the new FHA single-family suburbs, "hastening the decay of inner-city neighborhoods by stripping them of much of their middle class constituency" (Jackson, 206). FHA policies also supported and cemented the spatial separation of buildings and the segregation of use types. FHA requirements relating to minimum lot sizes, setback requirements, separation from adjacent structures and structure width "effectively eliminated whole categories of dwellings" (such as row houses) from eligibility from federal loan guarantees and what few multifamily developers the agency supported were pushed to suburbia: "Under the best of conditions a rental development under the FHA program is a project set in what amounts to a privately owned and privately controlled park area" (Jackson, 208).

At the same time that Roosevelt was working on financial solutions to the housing problem, his Public Works Administration (PWA) was experimenting with schemes more similar to the 'modern housing' proposed by liberal reformers. The PWA provided long-term loans with low interest rates to corporations and low-profit enterprises that were interested in producing modestly priced rental housing. The intent was to enable grassroots community groups to provide housing for themselves with support from the federal government. Though over fifty projects were constructed across the nation under this program, the PWA Housing Division did not last long. Many factors contributed to its demise; the government blamed greedy developers and developers blamed the PWA's overly centralized power structure and its director's "ironhanded" administrative style, but the program ultimately failed because during the Depression very few community groups were able to raise the funds necessary to participate (Radford, 105).

Because the PWA program had not made a serious dent in the housing problem and demand for affordable rental housing remained strong, the federal government decided, with the passage of the United States Housing Act of 1934, to build public housing. Early drafts of the legislation included progressive provisions for government-produced housing, but by the late 1930s “Better times [had] emboldened private operators to oppose any role in which the federal government might operate as a competitor” and by the time it was passed, the most reform-minded portions of the act had been compromised away (Radford, 180). All implementation decisions were left to the local level, where officials welcomed public housing with “the same enthusiasm as they might have greeted the introduction of bubonic plague” (Radford, 189). The act’s imposed cost limitations ensured that the housing projects constructed would be of low quality and that they would look unambiguously like poor people’s housing. This consolidated existing opposition to public housing projects and did not succeed in winning over any new supporters. Immediately following passage of the Act, business interests and the National Association of Real Estate Boards (NAREB) launched an offensive against the public housing constructed under the 1937 Housing Act, labeling it communistic. Their efforts were rewarded when anti-New Deal politicians elected between 1938 and 1942 continuously kept public housing spending levels low and banned the use any funds at all for public housing during World War II (von Hoffman, 304). During the war, very little housing was constructed and by 1949 Congress saw fit to pass more housing legislation. The Housing Act of 1949 restarted many programs from the 1939 legislation, including public housing. The act introduced urban redevelopment (now famously known as 'urban renewal') programs that mandated the clearance of 'blighted' areas by municipal governments or developers under contract to them. Thus the 1950s ushered in a second generation of public housing that incorporated ever-bigger apartment blocks and ever more experimental urbanism, eventually drawing vehement criticism from urban thinkers such as Jane Jacobs in her wrathful 1961 critique, *The Death and Life of Great American Cities*.

A 'TWO-TIER' POLICY

The housing policies adopted in the 1930s and 1940s and carried out through the 1950s and 1960s had a profound effect on the way Americans think and feel and about federal interventions in the housing policy arena. The series of acts created the "now-common two-tier pattern of well-legitimized, relatively generous support for the middle and upper segments of the population and poorly regarded, poorly funded programs for the least affluent" (Radford, 1). The first tier is the result of federal interventions in the financial markets such as the Federal Home Loan Bank Act, the HOLC, and the creation of the FHA. These policies are credited for revitalizing and modernizing the commercial housing industry, supporting social stability, increasing living standards, and creating an American commitment to homeownership. This tier specifically benefits the middle class and because it does not deal in direct subsidies, it operates largely out of the public eye. Because of this, the private market and Americans' ability to pull themselves up by their bootstraps have "received the bulk of the credit for the pleasant living conditions of the suburban neighborhoods in which the majority of American families now live," though the government played a significant role in shaping those living conditions (Radford, 203).

The second tier of housing policy in the United States is much more visible, consisting of direct assistance to the poorest Americans in the form of public housing projects built under the Housing Acts of 1937 and 1949. Public housing never enjoyed broad support, and very visible failures such as the dynamiting of the infamous Pruitt-Igoe project in the 1970s caused most funding sources to dry up. There is very little support in the United States for government programs aimed specifically at the poorest groups, especially when subsidies to the middle class escape detection. According to Radford,

> While using scarce public resources only for the most needy might seem fair and logical, programs limited to only the poorest turn out to have debilitating long-range problems. Their narrow constituency makes them more susceptible to budget cuts, and participants are often stigmatized (108).

Policies carried out though the 1960s left a lasting impression of publicly provided housing as badly managed failed experiments that were a waste of federal funds.

MODERN HOUSING POLICIES

As a result of its first tier successes and very public second tier failures, by the 1970s the federal government's Department of Housing and Urban Development (HUD) seemed to be "almost entirely out of the multifamily market" – no longer producing its own rental units, though still administering some voucher and block grant programs (DiPasquale, 101). In the last 30 years, HUD has instead turned its focus to developing first tier-type solutions to serve people at income levels not typically reached by previous policies. These solutions use financial and mortgage market mechanisms rather than brick-and-mortar development in an effort to leverage private investment, and to avoid the separation and stigmatization of populations that occurred in the much-maligned public housing projects.

The 1960s and 1970s saw the establishment of Government Sponsored Enterprises (GSEs) in order to facilitate the development of a secondary market for residential mortgages (HUD 2001). The Federal National Mortgage Association (Fannie Mae), though originally created in 1938 to purchase FHA-insured loans, was broadened and re-chartered in 1968, and the Federal Home Loan Mortgage Corporation (Freddie Mac) was established in 1970. While their charters specifically cover both single-family and multifamily mortgages, the GSEs' involvement in multifamily markets has historically run 20 to 30 years behind that in the single-family markets (Cummings and DiPasquale, 20). According to DiPasquale, "multifamily loans have historically represented a small portion of real estate loan originations and holding relative to single-family and nonresidential loans," and "despite growth in the 1980s, the secondary market for multifamily mortgages remains quite small" (79, 81).

After "Bloody Sunday" on October 6, 1979, when the Federal Reserve Board raised the discount rate by a full one percent in an attempt to ward off increasing inflation, interest rates climbed and "capital available for the commercial and residential real estate markets stopped flowing" (HUD 2001, 16). In an effort to provide incentives and jump-start real estate investments, Congress passed the Economic Recovery Act of 1981, which created incentives in the form of large and fast depreciation tax write-offs. This measure, along with interest rates that had started to fall in the early 1980s, opened the door to excessive overbuilding in multifamily markets across the country as investors developed projects with an eye toward tax benefits rather than market demand, resulting in shoddily-constructed apartment complexes full of empty units. According to DiPasquale, "there is no doubt that construction activity ran well ahead of demand in many parts of the country, and in some places, it oversaturated the market" (85). By the mid-1980s, "the volume of commercial real estate debt in portfolios became the largest in history (HUD 2001, 16). Congress intervened in 1986 with the Tax Reform Act, described in detail by DiPasquale and Cummings (1992), which greatly decreased the tax advantages associated with speculative investment in commercial real estate, including multifamily projects. To remedy this loss of incentives for multifamily construction, the Tax Reform Act of 1986 introduced the Low Income Housing Tax Credit (LIHTC), which since that time has become “the de facto federal low-income housing supply program” (Segal, 63).

Current affordable multifamily housing policy is a reflection of 60 or 70 years of federal interventions that prioritized single-family housing, relied on private capital to accomplish housing goals, and relegated multifamily housing to a second tier that never enjoyed much public support. The last few decades have seen first tier techniques expanded and put to work to encourage the construction of affordable multifamily housing. The next two chapters will look at the role of mortgage markets and the GSEs and the LIHTC in that construction, and more specifically at the impacts of those first tier techniques on the size of apartment developments.

Chapter 4: Barriers to Small-scale Development: Mortgage Markets and GSEs

As mentioned in the preceding chapter, the establishment of the Government Sponsored Enterprises (GSEs) around 1970 had a significant impact on markets in the United States. In the last 35 years, the mortgage market has grown from "a fragmented set of local credit markets to an important part of the national and international capital markets" (DiPasquale and Cummings, 77). However, the single-family-focused policies discussed in chapter 3 have resulted in two important gaps in financial markets where multifamily housing is concerned. First, credit for small multifamily mortgages is not always available on favorable terms. Segal and Szymanoski have found that credit gaps are particularly evident for multi-family properties of between 5 and 49 units, "possibly as a consequence of investor preference for larger properties with 200 or more units" (65). Second, the GSEs have not historically been very active in multifamily markets, and generally do not purchase small multifamily mortgages. Three-quarters of single-family mortgage originations are sold in the secondary market, compared to only about a third of multifamily mortgage originations (DiPasquale and Cummings, 77). Further examination by Segal and Szymanoski has revealed that "GSE multifamily mortgages tend to involve larger properties than are typical for the market as a whole" – in 1996 the average number of units in a multifamily transaction was 137 for Fannie Mae and 189 for Freddie Mac, but the overall market average was only 33 units (72). This chapter will look at how these two gaps in the market act as barriers to the production of smaller-scale multifamily developments, and will suggest ways to overcome the barriers and strengthen multifamily mortgage markets.

WHY SIZE MATTERS IN FINANCING MULTIFAMILY HOUSING

Before describing the market barriers to building small multifamily developments, it is important to understand that the availability and cost of financing for these projects is of particular concern because they account for a large share of the unsubsidized affordable rental housing stock. In its research the FHA discovered that the private housing market provides the majority of affordable rental housing in the United States, and that most multifamily rental properties are small projects in the 5 to 49 unit range (Schneider and Follain, 44). According to the Census Bureau's 1991 Survey of Residential Finance, 557,000 of the 633,000 multifamily properties in the United States have between 5 and 49 units, and the median rent at these properties is on average 16 percent cheaper than at larger properties (HUD 2001, 1). Segal and Szymanoski also found that properties of between 5 and 49 units are typically more affordable than larger ones (65). Though unsubsidized units in these projects often do not serve the very lowest income groups, they remain an important part of the affordable housing stock. Lack of available financing for these projects can lead to higher default rates, properties falling into disrepair because of insufficient maintenance, and the loss of affordable units as owners raise rents to support more expensive debt (Schneider and Follain), depleting an important share of the affordable housing stock.

It should be mentioned briefly here that parts of this chapter refer to small loans or mortgages in terms of their dollar value, as well as small projects, defined by their number of units. For the purposes of this report – dealing as it does with affordable housing and not small luxury rental products, loan value can be considered a proxy for development size and these concepts can be used interchangeably.

BARRIERS TO FINANCING

Research by HUD in 2001 speculated that the owners of smaller-scale properties may not always be interested in financing – that they may be able to finance their properties without significant debt (5). Though this may be true for some, such owners are not representative of the whole picture. Through interviews the same HUD study found anecdotal evidence of a credit shortage for smaller properties. Other researchers support this finding: Schneider and Follain found that while demand is high, "long-term sources of financing for this rental housing stock are not readily available" and that "financing costs for existing mortgage products are high relative to financing for single-family homes and large multifamily developments" (45). Though multifamily mortgage lending increased in the 1990s, Segal still found significant credit gaps – "borrower demand exceeds the supply of available credit at prevailing interest rates" (65). Forces in the mortgage market have combined to make access to financing difficult for small multifamily properties. Barriers include the high up-front costs of loan origination, perceptions about the risks associated with small projects, and the lack of a presence in the market by Government Sponsored Enterprises (GSEs). This chapter will look at these barriers, review attempts to improve these markets, and suggest recommendations for the future of small multifamily financing.

UP-FRONT COSTS

Mortgage lenders often feel that loans for small multifamily properties are less profitable for them than larger ones, because though small and large properties require the same origination and loan servicing processes, lenders are compensated with fees set at a percentage of the loan balance, making large loans much more attractive (HUD 2001; Cummings and DiPasquale 1998). At the same time, many small project developers find that the rigorous origination process and high up-front fees involved are more than they can bear. Many lending programs require sophisticated record-keeping, including extensive documentation of income and expenses, and costly inspections by engineers, environmental assessors, and the like – costs that are not generally scaled to the size of the loan or the number of units in a project (HUD, 30). Small properties often turn to local depositories, some of whom have developed a method of using salaried workers (rather than those earning commission) dedicated to processing smaller loans using a more streamlined appraisal process (HUD 2001). However, obtaining credit from depositories can contribute to vulnerability for apartment owners in four ways: First, financing from depositories is more likely to be offered under unfavorable terms such as shorter loan terms and adjustable rate mortgages (Schneider and Follain, 48). Second, many local depositories make the borrower personally responsible for the loan to offset the risks incurred by a less rigorous process. In this way loans are much like a residential mortgage, focusing on the credit-worthiness of the borrower more than the value of the project (HUD 2001, 15-16). Third, local depositories are a narrower market, in which the borrower has fewer options. This lack of competition in the market can lead to a fourth vulnerability as owners are subject to increased interest rates. In 2001, HUD found that the smallest multifamily properties had the highest interest rates (9-13). These higher interest rates are due in part to this lack of competition, and in part to the need of local depositories to offset the simpler underwriting procedures and lower fixed costs they offer to borrowers looking for smaller loans. While it may always be more expensive to obtain small loans because of those fixed costs, HUD suggests that "an expansion of the number and type of lenders serving this market would create greater choice of loan type, allowing borrowers to select loans which are best suited for their tastes and circumstances" (34).

PERCEPTIONS OF RISK

Players in mortgage markets have long held the perception that multifamily mortgage markets are unstable and that smaller properties represent an even greater credit risk and result in default more often than larger properties. One explanation for this perception is that occupancy rates can cause more pronounced revenue fluctuations in smaller developments. Two vacant units at a 10 unit property results in the loss of 20 percent of revenue, while larger developments are more insulated from occupancy rate fluctuations. Lenders are also concerned about the property management sophistication of small scale owners and their ability maintain their properties well. Third, in the case of foreclosure on a loan, the costs to the lender associated with that foreclosure consume a larger portion of the loan balance than they would if the loan were larger (HUD 2001, 18). Despite these concerns however, "neither a review of the literature nor interviews with lenders found any support for the view" that small multifamily property owners are a greater mortgage risk than larger ones (HUD 2001, 18; Schneider and Follain). Some authors think that small multifamily property owners may even be less likely than large property owners to default on loans because the property represents a large percentage the owner's assets, and because many have loans made by depositories for which owners are themselves directly financially responsible, contributing to "tenacity" on the part of the owners to make their project succeed (Schneider and Follain, 49).

In mortgage lending, "investment decisions are often based on perceptions rather than on facts" (Dipasquale, 78). A lack of data and a lack of understanding of the multifamily market causes many to believe that it is inherently volatile and risky, but DiPasquale suggests that the management and implementation of particular programs are to blame, and that "special expertise in underwriting and servicing can have a significant impact on multifamily loan performance," particularly for specialists in low- and moderate-income housing whose social goals make them more invested in the success of their projects (111-112).

LACK OF GSE LEADERSHIP

Perhaps the largest barrier to financing for small multifamily properties is the fact that though the Government Sponsored Enterprises (GSEs) purchase more small loans than the commercial market, they do not purchase small loans in the same proportion that small multifamily properties exist in the mortgage market (HUD 2001, 11). It is true that small loans do not lend themselves well to being purchased by secondary markets investors. This is due in large part to strict underwriting guidelines required by investors in order to accurately judge the quality of loans, which as mentioned above can incur often prohibitive costs to small property owners (Schneider and Follain), and to a lack of standardization among the loans, making then difficult to pool for sale in secondary markets. Despite these practical hurdles, HUD insists that

> The GSEs' failure to buy significant numbers of loans on small multifamily properties disadvantages the owners of such properties by denying them the benefits of mortgage liquidity provided by secondary market exposure to mortgages on larger properties (xvi).

The failure of the GSEs to participate significantly in multifamily markets is more than an inconvenience for project owners. According to Cummings and DiPasquale (1998), the GSEs were chartered to set up a secondary market for residential mortgage loans and to take a leadership role in the development of that secondary market. However, Segal and Szymanoski found in 1998 that "the GSEs overall approach toward affordable multifamily housing activities remains cautious" (60), and three years later HUD confirmed that the GSEs are "conservative and fairly inflexible, especially with regard to affordable properties" (xiii). GSE Fannie Mae's participation in the multifamily market is "dominated by activities in which it does not bear the risk of loss" (Dipasquale, 109). These assessments are particularly troubling because of the widely held belief that it is the responsibility of the GSEs to serve and develop underserved and underdeveloped segments of the mortgage market. Segal and Szymanoski note that GSEs "enjoy a substantial funding cost advantage relative to other entities as a consequence of their agency status" and therefore "have the ability to lead the industry" (68). Cummings and DiPasquale (1998) emphasize that GSEs have significant advantages over other investors, such as being exempt from state and local taxes. They also enjoy "the widely held view in the marketplace that in the event of financial problems the Federal Government will bail out either institution", despite the lack of any explicit guarantee to that effect (22). All this underscores the public-purpose mandate of the GSEs' charters. Not long ago single-family markets were seen as insurmountably heterogeneous and lacking in standardization, the way multifamily markets are now perceived. The standardization of these markets, spearheaded by the GSEs, took years. Many now believe it is time for Fannie Mae and Freddie Mac to commit to supporting multifamily markets in general and small loan markets in particular.

ATTEMPTS AT CHANGE AND CONCLUSIONS

In the 1990s, the GSEs and the FHA responded to critics and experimented with small loan products, but with limited success. Fannie Mae's Enterprise Mortgage Investments (EMI) and Freddie Mac's Local Initiatives Managed Assets Corporation (LIMAC) were small, understaffed programs that offered limited product. Separation from the larger GSEs and their resources impeded the financial viability of these programs: "The LIMAC and EMI experiences suggest that running a national program focused on small affordable housing transactions with a GSE is a difficult task for a small, under-staffed, undercapitalized, startup organization" (Cummings and DiPasquale 1998, 36). The FHA's Small Projects Processing (SPP) was designed to expand the FHA's largest multifamily programs into "project sizes not typically served by FHA multifamily insurance programs" (Schneider and Follain, 44). Unfortunately, SPP has run into budget constraints similar to the GSEs' programs and it's limited funding precludes any sort of evaluation component. So far, the effectiveness of these programs and their real impact on the market is hard to judge. The HUD report worries that "according to informants, some of these programs gain high visibility in the press but are seldom used in the marketplace" (xx). Nevertheless, these programs are working to clear away "lingering perceptions of small multifamily loans" as volatile and prone to default (Schneider and Follain, 56).

In conclusion, financing for small multifamily development is available in mortgage markets, but is rarely offered on favorable terms and does not enjoy the support of a strongly GSE-backed secondary market. There is significant room for expansion in this sector of the market, and GSEs have an obligation to support because evidence shows that small multifamily developments are more affordable on average than larger ones.

Chapter 5: Barriers to Small-scale Development: The Low Income Housing Tax Credit

The previous chapter looked at how barriers relating to mortgage markets and the GSEs have kept multifamily housing (and especially small projects) from benefiting from the 'first tier' housing policies enjoyed by single family housing in the United States for the last half-century, and looked at ways that bias is slowly being remedied. The Low Income Housing Tax Credit (LIHTC), though also a first tier-type strategy that leverages private investment by relying on money markets, is a much more direct policy – one specifically targeting low-income households and aiming for a deeper affordability than even GSE-supported markets could provide. As related in chapter 3, the LIHTC was implemented in the Tax Reform Act of 1986 after it was realized that all incentives promoting the construction of affordable multifamily housing had evaporated as tax code loopholes were closed. Since then, the LIHTC has been the most dominant source of funding for affordable multifamily housing in the US (Pagano). It is the "single most important source of equity for low-income rental housing in the United States" (Schwartz 2006, 98) and has been described as "the current standard approach" to producing low-income housing (DiPasquale, 88) and "the de facto federal low-income housing supply program" (Segal, 63). The LIHTC is without a doubt the most important affordable housing resource, leading to nearly 25,500 projects and over 1,415,000 housing units placed in service between 1987 and 2004 (HUD 2007).

How it Works

The LIHTC is a complicated system of tax credits and regulations, administered by both the Internal Revenue Service (IRS) and state housing agencies. The IRS issues a dollar value of available credits to the state housing agencies based on state population using a per capita allocation that is indexed to inflation (in 2005 the credit was $1.85 per person). State agencies then award the credits to developers of affordable housing based on Qualified Allocation Plans or QAPs – state-specific rubrics on which the merits of applications for the tax credits are judged. At least 10 percent of a state's credits must be allocated to non-profits developing housing. Developers, often nonprofits, generally sell their credits to a syndicator, who can use the credit as a dollar-for-dollar offset against other taxes to be paid, which provides the equity to developers to actually finance the projects. In the early years of the LIHTC program syndication fees ran as high as 27 percent but since then have declined dramatically, from 10 to 14 percent in the mid-1990s to about 6 percent now (Schwartz 2006, 87). Properties financed through the LIHTC must comply with income requirements from the federal government, containing at least 20 percent of units affordable to those with an income at or below 50 percent of the Area Median Income (AMI), or at least 40 percent of units for those at or below 60 percent of AMI.

The IRS enforces the tax code while the state housing agency monitors compliance with income requirements.

THE SIZE OF TAX CREDIT PROJECTS

According to the U.S. Department of Housing and Urban Development's Office of Policy Development and Research, while the number of Low Income Housing Tax Credit projects built per year has remained fairly steady since the program's inception, the number of units produced has risen continuously (2004). Schwartz also reports a steady increase in the size of LIHTC projects, from an average of 30 units in 1987-1989, 39 units in 1990-1993, 63 units in 1994-1999, 75 in 2000-2002 (2006, 91) – indicating that more larger apartment developments are being built with the LIHTC. Schwartz calculates an overall average project size of 52 units for the 21,953 developments with 1,141,650 units placed in service between 1987 and 2002. A look at LIHTC information from HUD for projects placed in service most recently (from 1995 to 2002) shows that the largest projects are concentrated in the South and West regions of the country, where at 84 and 80 units respectively, average project size exceeds the national average during that time of 69 units (the Northeast and the Midwest come in below average with 52 and 56 units per project). These statistics show that LIHTC projects built in the South and West where land prices are cheaper and cities are less dense tend to be larger than the national average (Schwartz 2006, 93), and though this does not indicate that LIHTC projects are ballooning in size across the United States, it is an important finding. After all, it is in the South and West where this country is experiencing the highest levels of population growth and where thoughtful building can have the greatest impact. The next section describes some of the challenges within the LIHTC system and how it is administered that can work against the construction of smaller developments.

CRITIQUES OF THE LIHTC

One of the most frequently expressed criticisms of the LIHTC is that it is a complicated and transaction-intensive system. Initially in the mid-1980s, the program was slow to start, no doubt because of its very complex structure. In 1987, the program's first year, states allocated only 18 percent of their total authorization. Two years later developers of tax credit projects began to catch on and 98 percent of state authorizations were allocated (DiPasquale, 89). Though by this time many developers specialize in tax credit projects and confusion about how to do tax credit deals has diminished, DiPasquale points out that putting together a tax credit deal involves many players, complicated paperwork, and tricky financial arrangements – all leading to significant investments in lawyer and accountant hours (90). Susan Sheeran, of San Antonio's Merced Housing Texas notes that using the LIHTC is an expensive way to produce affordable housing, though it is one of the only ways available to do it. Beyond negotiating those costs, the affordable housing developer must still secure a conventional mortgage and most likely find gap financing from state, local and nonprofit subsidies, because the tax credit does pay for the full cost of development (92-93). Often, state housing finance agencies try to spread tax allocations out among projects, awarding less than the full amount of credits than a project is eligible for and necessitating further gap financing (Schwartz 2006, 88). These complicated deals are a particular barrier for small tax credit projects. Developers encounter the same mortgage lending barriers described in chapter 4 and must also contend with the disinterest of syndicators who prefer to purchase credits in larger volume from larger projects.

The involvement of investors and for-profit developers in the LIHTC program is also a factor increasing the size of projects. Walter Moreau of Foundation Communities points to his experience with developers looking to "do good by doing well" by build multifamily developments with over 400 units. Even nonprofit developers are often concerned with the quantity of units, wishing to provide affordable housing to the largest number possible, and understandably so. Unfortunately however, this push to produce a large quantity of units, coupled with LIHTC regulations about the quality of the interior of those units, can lead to an excessive focus on apartment units as individual consumer items, ignoring the neighborhood around the development and the fabric of the city. Put another way, "the LIHTC program is used much more often to provide better housing in poor neighborhoods rather than to provide affordable housing opportunities in higher-income neighborhoods" (Cummings and DiPasquale, 272). This finding takes on even greater implications if we think of these “higher-income neighborhoods” as areas of high opportunity under the Kirwan Institute’s Opportunity Mapping concept described in chapter 2.

Finally, due to the financing complexities inherent to the LIHTC program, developers often apply for credits for all units in a development rather than just the percentage mandated by the law, and developments end up with 100 percent of their units set aside for those with incomes at or below 60 percent MFI. Though “the program was designed to encourage mixed-income development, thereby avoiding the poverty concentration and isolation issues associated with public housing” in practice developments using LIHTC funding are “nearly always fully income restricted” (Tighe, 8). Developers interested in maximizing their credits and renting to a somewhat higher income bracket often create projects with all or nearly all their units set aside for low-income occupants. Cummings and DiPasquale found in their sample that 83 percent of LIHTC developments consisted of 100 percent affordable units (276), and Schwartz cites that on average 96 percent of apartments in tax credit projects are designated for low-income households and remarks that “the credit provides no incentive for developers to create mixed-income developments” (2006, 92-95). The LIHTC, especially in the West and South, results in large multifamily complexes (averaging over 200 units in Florida and 120 in Texas) that are both esthetically monolithic and homogeneous in terms of the population they serve.

CHANGES TO THE LIHTC AND CONCLUSIONS

Because individual states decide how to allocate their tax credits, it is the state QAPs that hold the key to shaping the development of tax credit properties. HUD's 2002 Analysis of State QAPs suggests that in the 1990s states "became more precise in specifying preferred building preferences" including the size of developments (15). California is one state that caps the size of tax credit allocations in order to try to reduce the size of projects (Ferguson). Though California's 96-unit average project size is significantly smaller than other large and growing Sunbelt states Texas and Florida, it is still well above the national average (HUD 2004). HUD's 2002 analysis does point toward a general trend of states using their QAPs to more actively restrict project sizes in recent years. Recommendations from the Poverty & Race Research Action Council (2004) suggest that state QAPs should go further to encourage different development. Recognizing the steep transition costs of putting together a tax credit deal, the Council argues that "more flexible site control and financing standards should be adopted for scattered site developments, so that they are financially competitive with larger single-site developments" and that "tax credit programs should be combined with land write-down programs to acquire development sites in lower poverty areas."

There are examples of developers who have managed to fund smaller-scale scattered site affordable housing developments. Developer Ike Monty in El Paso, Texas has managed to bundle projects, selling tax credits to one person for three or four projects consisting of 30 to 50 units each. But Walter Moreau, executive director of a nonprofit housing organization that also uses tax credits suggests that Monty's experience in El Paso is the exception to the rule, remarking that it can be done only "if all of the projects were using the same basic financing scheme and if timing coincided" and mentioning that Monty is a well-known and high-volume developer who wields a certain degree of influence in El Paso, which perhaps greases the wheels to see his unconventional tax credit deals through.

It is clear that the Low Income Housing Tax Credit program is facilitating the development of large-scale multifamily developments in the booming areas of the South and West. As the institutional know-how about the complicated nature of the LIHTC process has increased and the tax credit program remains the most important source of funding for low-income housing, it is time to be more aware of the form of the projects it builds. States should continue to restrict the size of allocations in order to encourage smaller developments. QAPs should also be amended to give greater weight to the location, density, and design of projects, as well as their accessibility to jobs, transit, and schools. Most importantly, policymakers must find a way to codify the use of tax credits to support the sort of scattered site development that Monty was able to put together in El Paso. Without changes in policy the LIHTC program will continue to support the production of large apartment complexes built on greenfield sites, the form of which preclude the existence of an urban form that lends itself to coherent neighborhoods, human interaction, and adaptability.

Chapter 6: Barriers to Small-scale Development: A New Model for CDCs

Though mortgage markets and the Low Income Housing Tax Credit are important factors limiting the development of smaller-scale multifamily developments, organizations that build these developments merit closer study. For decades, nonprofit community development corporations (CDCs) have been involved in the production of affordable housing rental housing, but shifts in housing finance policy and demography are changing the way CDCs work. This chapter will look at the development of CDCs since the 1960s, discuss the ways in which CDCs following the original model differ from those coming about in a new context, and will discuss emerging strategies to promote small-scale multifamily housing, even given the new environment of many of today's CDCs.

THE DEVELOPMENT OF CDCS

The term "community development corporation" is used to describe nonprofit organizations that that support low-income communities by engaging in a variety of activities, including housing, economic development, job training, and education. For the purposes of this report, I will use the term to refer to those whose primary work is the provision of affordable housing though they may also offer other services. CDCs first came about in the 1960s, emerging from a set of social and political circumstances that included President Lyndon Johnson's War on Poverty, the civil rights movement, response to federal urban renewal programs and disinvestment in public housing (Vidal, Briggs and Mueller, Schwartz, TACDC). Many of these early CDCs were initially funded through the federal government's Equal Opportunity Act's Special Impact Program or the Model Cities Program (Vidal, 34). The Community Revitalization Act (CRA) of 1977 encouraged the establishment of CDCs by pumping investment from banks into CDCs and the poor neighborhoods they supported, and during the 1990s the Community Development Block Grant (CDBG) and HOME programs helped sustain CDCs financially (TACDC). Most established CDCs have followed a model that came out of the experience of neighborhood groups focused on revitalization in the large cities of the Northeast and Midwest with a mission to serve "geographically defined communities, i.e., neighborhoods" – specifically neighborhoods economically disadvantaged in comparison to other areas of their cities (Vidal, 3). Vidal found that CDCs serving a larger area were atypical and Briggs and Mueller's study echoed that CDCs are "commonly defined by a spatial focus" (1). Vidal notes that "community-based development as an urban phenomenon has a stronger tradition and is more widespread in the older cities of the Northeast and the Midwest then in cities in the West and South" – cities such as Boston and Chicago are known for their "strong neighborhoods and active CDCs" (24). Large cities in the Northeast and Midwest have historically supported more

CDCs than cities in the South and West, saw the highest growth in the number of CDCs (in both absolute and percentage terms) at the time of Vidal's research in the late 1980s, and now some 25 years later still contain more CDCs than cities in other regions (Schwartz 2006). Though most of these CDCs are small, working with limited staff and on a modest financial scale, Vidal found that they do manage to produce a significant amount of affordable housing. CDCs have taken up where the federal government's public housing programs left off, and produce well above the federal government set-aside for community housing development organizations. However, the number of units produced still does not meet the demand for affordable housing (Vidal, 87), and it is not clear that this CDC model is appropriate for growing cities in the nation's Sunbelt South and West.

A NEW CONTEXT

Schwartz reports that in the first three years of this decade, the South and West accounted for almost 70 percent of all new owner-occupied and rental units built (2006), and though this statistic does not refer specifically to affordable housing, it clearly shows where growth is occurring in the United States. As population growth concentrates in the South and West, the same need for affordable housing, economic development, and social services experienced by neighborhoods in the Northeast and Midwest is emerging in a new urban context. Briggs and Mueller pointed out that "the strategies that CDCs choose to emphasize and the successes that

CDCs have are powerfully shaped by the local demographic, institutional, and political context" in which they are found. Vidal's research supported this statement with a specific example, finding that the presence of distinctive, well-defined neighborhoods in a city contributes to an urban environment conducive to community-based development, and that of the ten sample cities that had few well-defined neighborhoods, seven were located in the West or South (105-107). Though neighborhood-based CDCs do exist in these regions of the country and have produced affordable housing that fits very well into existing neighborhoods (see Blackland CDC and the Guadalupe Neighborhood Development Corporation in Austin, Texas for two examples) the limited number of strong, distinctive neighborhoods in the South and West suggest that this model can have only limited effectiveness in today's growing cities.

So what can we expect to see from this new generation of CDCs working in a very different urban landscape? An example from Texas points to some interesting trends. A report from the Texas Association of Community Development Corporations shows that though larger scale CDCs producing a significant volume of housing constitute the smallest share of CDCs, they produced 76 percent of the rental units built between 2000 and 2003. A report from the National Congress for Community Economic Development confirms this trend, noting that "the percentage of CDCs that have become large-scale housing producers has risen significantly" over the years (11).

For some CDCs working in Sunbelt cities, a new model based more on local real estate trends than on any specific neighborhood is taking hold. Schwartz classifies these organizations in a category distinct from traditional neighborhood-based CDCs, calling them “large citywide or regional housing organizations”. Foundation Communities in Austin, Texas is one such organization, having produced over 2000 units all over Austin and in the Dallas-Fort Worth area. Foundation Communities’ executive director Walter Moreau explains that the organization’s “development prospects have always been opportunistic” and though “the planners hate it”, the organization works in “real estate and it’s expensive and we need to think about the market.”

Though these citywide or regional housing organizations exist in the Northeast and Midwest, their lack of focus on any one existing neighborhood make them a particularly good fit for recent-growth Sunbelt cities that lack large numbers of coherent neighborhoods. Because they are not trying to fit into established areas and because they operate in newer cities with large tracts of available land, there is a tendency for these larger real estate-based CDCs to build bigger developments. This is reinforced by strategic development reasons to build on a larger scale. Mike Clark with Alpha Barnes, a property management company that works with nonprofit housing organizations, calculates that 70 apartment units will support a full time maintenance person, and Walter Moreau at Foundation Communities uses a similar formula, estimating that between 70 and 100 units will support a full time manager and maintenance person, though this figure depends on the age of the property, its compliance requirements and its rate of turnover. Smaller projects present challenges and require more innovative solutions. Moreau described the management difficulties Foundation Communities has experienced at Daffodil, its smallest property at 42 units – the property has had one person responsible for both management and maintenance, has operated with onsite part time resident staff, and is now sharing management and maintenance personnel with another property several miles away. Merced Housing Texas in San Antonio has had a similar experience trying to efficiently staff two small apartment complexes in the same neighborhood. Mr. Moreau also stressed that "the same economies of scale ring true on the development end as well" because it takes the same energy and staff time put together a project with 20 units as one with 100 units, especially in the face of limited funding.

The traditional CDC model focuses on a holistic vision of neighborhood revitalization, something that new larger-scale housing organizations hope to maintain by offering social services in conjunction with affordable housing. Affordable housing providers across the country have adopted a model that includes a host of adult and children's programs, often held onsite in learning centers at apartment properties that include computers labs and classrooms, and are generally staffed by service coordinators. These services provide three benefits to affordable housing providers. First, they fulfill a mission of the housing organization and allow nonprofits that focus on housing to serve their residents in myriad ways. Second, the services are an amenity that attract resident to the property. Third, the services are appealing to funders such as private foundations who may not be interested in affordable housing but are more than willing to support a children's afterschool program, or believe that their funds will "teach a man to fish" through adult education. This model has an enormous affect on the size of projects that interest many affordable housing developers. To cover the cost of a full-time service coordinator and to achieve a critical mass of children and families for the programs offered, an apartment development must have around 150 units, explains Foundation Communities' Executive Director Walter Moreau. He explains that these "economies have driven the size of our properties more than anything else". Frances Ferguson, a founder of Foundation Communities and current Director of the NeighborWorks Multifamily Initiative agrees: "my personal experience is that larger projects are more successful… Personally, I believe that 100 to 200 units is a nice size because it supports better services".

Without a commitment to a particular neighborhood, the new, larger, real estate-based CDCs often focus on issues such as the economies of scale presented here to steer their decision-making. This often results in developments of a larger scale than are typical in a traditional CDC context, where location matters more than the number of units in a development and social services can be provided in the community without being located at a particular property.

FUNDING FOR HOUSING CDCS

Research has documented the success of CDCs in producing small-scale multifamily development for decades, but will changes in the affordable housing funding paradigm affect the housing product of CDCs? CDCs receive funding from various sources, including federal government programs, the LIHTC and state housing agencies, local government housing finance corporations, corporations, foundations, and private donations, and each source involves its own rules, regulations, and transaction costs that affect the size of development projects. Vidal found that cities with more financial support from local government, foundations, and the private sector tend to have more CDCs that tend to be more active than those in cities lacking this type of support (12). These CDCs have entered a cycle where "success breeds success" using local government and private funding to build a track record that will allow them access to more funding (12). Also, according to Vidal's study, nationally 78 percent of CDCs receive significant funding from the federal government, and this funding totaled one-third of the unearned income of CDCs studied (3). Returning to the Texas example, we find that state and local government sources of the sort that encouraged active CDCs in Vidal study account for only 1.4 and 1.1 percent of development funding respectively, while the LIHTC and 501(c)(3) Bonds accounted for 31 percent, and federal sources such as HOME and CDBG another 12.5 percent (TACDC). Vidal found that the age of a CDC may also affect the sorts of funding it receives; in his study 52 percent of CDCs over 16 years old (in the late 1980s) received state funding, compared to only 32 percent of younger CDCs, with similar results for local funding. Though Vidal did not provide information regarding the age of CDCs by region, the TACDC report confirms that most Texas CDCs were founded later – 63 percent were established in the 1990s and another 9 percent were established between 200 and 2003. All of these figures suggest that CDCs in Sunbelt cities lack the sort of flexible local and private funding that are available where CDCs are older, more common, and better established.

Much more research is required to determine exactly how funding sources available to CDCs affect the sort of housing they are able to produce. If federal sources such as CDBG continue to become less available (Schwartz), CDCs in cities with weaker neighborhood and CDC traditions who do not receive large amounts of local and private funding may have to rely increasingly on programs such as the LIHTC, which, as we saw in chapter 5, carries its own constraints in terms of producing smaller-scale apartment developments.

EMERGING STRATEGIES

How in this new context can CDCs continue to produce small-scale multifamily housing developments while maintaining a holistic focus and holding true "to the kind of comprehensive agenda and mission of their 1960s roots" (Glickman and Servon, 241)? Often, operating social services such as afterschool programs are a financial strain for affordable housing providers. One solution is to rely on other more specialized agencies by engaging in partnerships. Foundation Communities in Austin is currently discussing the cost burdens associated with running some of its children's programs, and is looking at expanding its partnership with a nonprofit provider of afterschool care to provide services to more of its apartment properties.

Beyond partnering to provide services onsite at their apartment properties, CDCs can also establish relationships with organizations that use facilities already present in the community. The federally-funded 21st Century Community Learning Center program, and others such as the San Francisco's Beacon Initiative, take advantage of the brick and mortar resource provided by neighborhood schools and use them when the school day is over as sites for afterschool programs and continuing education classes for parents and families. The per-participant cost of these programs is certainly comparable to (if not lower than) the cost of running a learning center onsite at an affordable housing community (Keane). Using schools in this manner would promote neighborhood schools as symbols of learning and hubs of community activity, and would allow CDCs with similar goals to share resources.

The new generation of citywide and regional housing organizations should look more closely at traditional neighborhood-based CDCs and consider that the provision of social services is but one element of successful, holistic affordable housing provision. The integration of that housing with strong existing neighborhoods is perhaps an even more important element that today's real estate-based housing organizations should seek to achieve.

Chapter 7: Conclusions and Recommendations

As this report has shown, large-scale affordable housing apartment developments are becoming more and more common, especially in the high-growth West and South, but do not serve their residents in the best way possible. Problems with these developments became apparent in 2005 when thousands of New Orleans residents came to Austin after fleeing Louisiana in the wake of Hurricane Katrina. Though many of the families that moved into apartment complexes around the city came from neighborhoods of high poverty and frequent violence, their new living situation presented them with new problems. From the Austin American-Statesman article “Evacuees in suburbia”:

> There is no bus stop here. The nearest supermarket is a $20 cab ride away. It's a long haul with groceries for 8-year-old Tatyana Thompson. She and her parents take a $20 cab ride from their Eagles Landing apartment on Decker Lane to a Wal-Mart to stock up on food. Many evacuees landed in Austin without cars and are now far from services… As many as 7,300 hurricane evacuees are now in the Austin area, and many live along the city's newest fringes in apartment complexes that, for the very reason of their remoteness, had vacancies before the evacuees came along… The apartments here,

> plopped down in the middle of nothing, might be called formless were it not for their relentless repetition…"The first day, we loved the apartments," said [Stephanie] Gleason, a 31-year-old mother of three boys, the oldest of whom takes a taxi to McCallum High School at least 10 miles away. "Now I feel so isolated"… The isolation hampers the evacuees' access to the social services they may need and hinders their job-hunting prospects.

Along with changes to the mortgage lending system and the Low Income Housing Tax Credit and a shift in the way CDCs operate, a more fundamental change in thinking must take place in order to support a smaller-scale model of affordable housing: policy makers and developers of affordable housing (especially those that employ a real-estate based model of development) must gain a greater awareness of physical planning and must consider more carefully the myriad impacts their projects have on residents and the form of cities alike. They must consider the quality of units in terms that go beyond ceiling fans, pools, and learning centers.

Ben-Joseph believes that planners in general have shirked their duty to advocate for and inform about physical design:

> The planning profession has generally been reluctant to champion physical design, largely because of an ideological commitment to social science-based discipline as the foundation for urban planning education and practice. This

> has resulted in the marginalization of urban design and physical planning to the point that it all but disappeared from urban planning curricula.

However, we now see “a renewed emphasis on place and ways of living has brought urban design to the forefront” of planning thought (115). Planners must now work to bring physical planning together with social science, advocacy, and policy, to work on developing affordable housing that reduces costs to the residents and creates value for the greater public.

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